THE COUNTY OF BERNALILLO

Description of Bonds and Incentives

INDUSTRIAL REVENUE BONDS IN BERNALILLO COUNTY

IRBs

An IRB is a loan by a lender/bond purchaser to a company, where the loan proceeds and the loan repayments flow through a governmental "issuer." An IRB involves a company (a corporation, a partnership, or a sole proprietor) which wants to purchase and/or construct and/or equip a facility. Instead of purchasing, constructing, or equipping the facility directly, the company enters an agreement (usually a lease) with the issuer. The agreement provides that the company will lease the facility from the issuer and, at the end of the lease term, purchase the facility for a nominal amount. Acting in the capacity of an agent, the issuer agrees to purchase, construct, or equip the facility.

In order to obtain the funds to complete the agreement, the issuer will generate the bonds. The proceeds of the bond sale pay the expenses of the facility. The rent paid by the company to the issuer will pay off the issued bond amount. The tax benefits of IRBs result from the loan and involvement of the issuer.

Benefits

Industrial revenue bonds (IRBs) have three principal benefits for companies:

1. Property tax exemptions (Land, buildings and equipment associated with an eligible project are exempt from ad valorem tax for as long as the bonds are outstanding, up to 30 years);
2. Gross receipt tax exemptions or Compensating Tax Abatement (Furniture, fixtures and equipment purchased with industrial revenue bond proceeds for an eligible project are exempt from gross receipts tax if purchased in the state and compensating tax if purchased out of state), and
3. Lower interest rates than other types of borrowings.

The first two are usually available. The third depends on the IRBs being "tax exempt," which is rare.

Issuers

Bernalillo County can issue IRBs for projects within both the unincorporated area and municipal limits.

Projects

IRBs can only finance "projects" that include land, buildings, furniture, fixtures, and equipment. Projects do not include facilities for the sale of goods and services at retail. Projects do not need to include land; they can be for equipment only. Any land included in a project does not have to be owned in fee. The financed costs of projects are limited to capital costs and transaction costs. IRBs generally cannot finance working capital.

Property Tax Abatement

Equipment, real and personal property included in a project financed with IRBs is exempt from property tax for as long as the bonds are outstanding, up to a maximum of 30 years. The property tax exemption results from the fact that the issuer holds title to the project property, and the New Mexico State Constitution exempts taxation of county property. Issuers may require "payments in lieu of taxes" or may shorten the bond term, thereby decreasing the benefit of the property tax exemption.

Gross Receipt Tax Exemption

Furniture, fixtures, and equipment purchased with IRB proceeds for a project is exempt from gross receipts if purchased in the state are exempt from compensating taxes if purchased out of state. The exemption results from issuer holding title. For the exemption of gross receipt tax, a nontaxable transaction certificate is required. Building materials incorporated in a project are not exempt from gross receipts and compensating taxes. An additional investment tax credit may be available for manufacturing equipment, depending on the number of new employees related to the project. If an IRB structure is not used, the tax credit merely offsets the compensating tax or a portion of the gross receipt tax imposed on equipment. Similarly, if an IRB structure is used, the gross receipt or compensating tax is avoided and the credit can be applied to other taxes, such as payroll withholding taxes.

Tax Exempt IRBs

Interest on New Mexico IRBs is exempt from New Mexico income tax. In order for interest on IRBs to be excludable from gross income for federal tax purposes (i.e., "tax exempt"), several conditions apply. Most importantly, the project must be a manufacturing facility. No "substantial user" of the project (including the company) may make more than $10 million in capital expenditures (whether or not related to the IRB project) within the boundaries of the issuer in the six-year period beginning three years before the date the bonds are issued. "Tax exempt" IRBs will carry a lower interest rate than similar "taxable" IRBs, often about 30% lower. Because of tax provisions that do not allow banks to deduct their "costs of carry" with respect to IRBs, there is generally no interest rate difference between similar "taxable and "tax exempt" IRBs sold to banks. "Tax exemption" is lost if the IRBs are held by an affiliate of the company

Credit Considerations

An IRB does not put the issuer's credit on the line, only the company's. The issuer is only a conduit, agreeing to pay the bondholders only what it receives from the company. Therefore, if a lender would not be willing to make a loan to a company, that lender generally will not purchase IRBs issued for that company. IRBs can be backed by "credit enhancement," such as a guaranty, a letter of credit or an insurance policy. However, if a "credit enhancer" is not willing to make a loan to a company, that credit enhancer will not be willing to issue a letter of credit, guaranty or insurance policy backing that company's IRBs. If a lender is willing to make a loan to a company, that loan can generally be structured as an IRB. Many "taxable" IRBs are structured to be purchased by an affiliate of the company (often called "self purchase").

Timing

From start to finish, the issuance of IRBs by generally takes at least eight-ten weeks. Because of additional statutory notices and waiting periods, New Mexico Counties take at least four additional weeks to issue IRBs. These minimum times apply to "self purchases." If a third-party lender is involved, several more weeks should be added; if a credit enhancer is involved, there will be an even longer period.

Approval

The Bernalillo County Commission approves Bernalillo County IRBs. The officials involved will be weighing the costs and benefits of the IRBs. The chief cost consideration is foregoing tax revenues (in some cases, th*e* project would not be undertaken without the IRBs) so there is little tax loss. The chief benefit is usually job creation, the more the better. It is often difficult to get IRBs issued for an existing facility, unless the facility would close without the IRBs. IRBs are unlikely for facilities that compete with existing businesses. Officials are sensitive to environmental issues surrounding the project and to the concerns of neighbors and neighborhood impacts. County officials are also interested in the creditworthiness of the company. Although the issuer's credit is not on the line, default is embarrassing to the issuer.

Savings and Costs

On a $3.5 million project consisting of $.75 million in land, $.75 million in buildings and $2 million in equipment, the present value of the property tax savings over 20 years is roughly $150,000. (A 19-mill property tax rate, a 20-year life for equipment and 30-year life for the building, with straight-line depreciation with present value calculated on an 8% discount rate). The compensating tax savings on the equipment are $100,000. (This assumes all will be purchased out of state; if purchased in state, the gross receipts tax savings are slightly higher.) If the equipment is manufacturing equipment, an investment tax credit of $100,000 is available.

If the IRBs are "tax exempt," the present value of the interest savings could amount to $1.3 million (based on annual interest rate of 5% as opposed to 8%, over 20 years, again discounted to present value at 8%).

On the cost side, the transaction costs for a simple "self purchase," which include the fees of lawyers for the company and issuer, are roughly $15-25,000. For a "tax exempt" transaction, the costs would be $35-50,000. If the County of Bernalillo requires intensive staff review or outside review, add $5,000-10,000. For credit enhancement, add another $10-15,000 in transaction costs and 1-1.5% of the principal amount in annual expenses. These expenses are in addition to those involved if IRB's are not used. For example, private financing would involve title insurance premiums, legal fees associated with the purchase or long term lease of real estate, and legal fees related to the negotiation of loan documents, as well as other secondary costs. As a rule of thumb, "self purchase" IRBs generally are not cost effective for projects of less than $750,000 and "tax exempt" IRBs are not cost effective for projects of less than $1.5 million.

IRB Caution

Companies considering IRBs should not to commit to legally binding contracts, except on a contingent basis, until an IRB inducement or ordinance approval by Bernalillo County. Transactions of this type, made before IRB inducement and authorization, should have a provision that clearly states that the offer is contingent upon issuance of the IRBs.

This rationale is to allow a company sufficient flexibility in the transaction before official governmental action. Furthermore, companies should not assure the development of a project (by action or perception) regardless of the decision of Bernalillo County Government**.**

Miscellaneous

A developer can use IRBs. Bernalillo County can issue a separate series of bonds to finance the developer's real estate and building costs. The tax savings of the IRB can flow through to the ultimate user through a sub-lease. In event of sale or lease to new user, the benefits of remaining property tax exemption go to the new owner or flow-through a lease.

INCENTIVES IN BERNALILLO COUNTY

In-Plant Training and Tax Credits

INDUSTRIAL DEVELOPMENT TRAINING PROGRAM (IN-PLANT) IN BERNALILLO COUNTY

In-Plant Training

The Industrial Development Training Program (In-Plant) is a state program utilized by Bernalillo County. It provides pre-employment, classroom, and on-the-job-training and funds to a corporation or institution. The purpose is to prepare New Mexico residents for full-time employment. It is highly flexible and well funded by the New Mexico State Legislature. Post-secondary educational institutions, company trainers, and outside trainers can provide the customized training. When classroom training is provided by a public training institution, 100% of the training cost is reimbursed to the institution. The state will reimburse:

1. 50% of trainees' wages up to 1,040 hours in urban areas and 75% of trainees' wages in rural areas.
2. 80% of trainees' wages up to 1,040 hours in rural areas if company has fewer than 20 employees, such company is also eligible for modified/short form proposal; or
3. 90% of trainee's wages up to 1,040 hours if company is located in an economically distressed area and has fewer than 20 employees.
4. 50% of trainees' travel and per diem for out-of-state training (65% in rural areas).
5. 50% of company or outside trainers' travel and per diem when using out-of-state trainers.

Conditions:

A. The maximum wage reimbursement associated to the hours required to learn job and hourly wage.
B. Applicants must be New Mexico residents for one year.
C. Full-time year-round employment upon successful completion of training guaranteed to trainees.
D. Hands-on" or production jobs qualify; supervisory, salaried or professional jobs do not qualify.
E. The In-Plant Training Board is using the *Directory of Occupational Titles* to determine the maximum allowable training hours for a position. Proof of actual training hours will be required.
F. Retraining is not qualified for assistance.
G. Companies can apply for subsequent assistance if they have maintained hiring levels that exceed the peak employment as established by the initial application.

TAX CREDITS IN BERNALILLO COUNTY

Child Care

New Mexico law provides for a Corporate Income Tax Credit of up to 30% of eligible expenses, net of reimbursements for child care services incurred and paid by the taxpayer in the taxable year for dependent children of their employees. A taxpayer that operates a child care facility used primarily by the dependent children of the taxpayer's employees may also claim a Corporate Income Tax Credit of up to 30% of the net cost of operating the child care facility

Conditions:

A. Dependent children under 12 years of age.
B. Credit may not exceed $30,000 in any taxable year and unused credits will carry forward for three consecutive years.
C. Any receipts of a corporation from an employee for the use of the childcare facility is considered a reduction of the allowable expenses for computing the child care credit.

Manufacturing Investment Tax Credit

New Mexico tax law provides for a credit equal to 5% of the value of qualified equipment and other property used directly and exclusively in a manufacturing operation. Purchase price or book value of the equipment is used to determine the amount of the credit. The credit is against compensating or gross receipt tax or withholding tax due. The credit is limited to 85% of the sum of the taxpayer's gross receipt tax, compensating tax, and withholding tax due for the reporting period. A Company can claim any remaining available credit in subsequent operating periods.

The credit applies to purchases made before 1/1/2004 and must meet the following criteria for new jobs added: (a) 1 job/$250,000 for first $2,000,000 of equipment; (b) 1 job/$500,000 for next $28,000,000 of equipment; (c) job/$1,000,000 for equipment over #30,000,000

New Mexico State Statute defines qualified equipment eligible for the manufacturing investment tax credit as (NMSA 7-9A-3B):

> Equipment means an essential machine, mechanism or tool, or a component or fitting thereof, used directly and exclusively in an manufacturing operation and subject to depreciation for

purposes of the Internal Revenue Code by the tax payer carrying on the manufacturing operation.

This does not include vehicles. If the equipment is a true lease, the company cannot take the manufacturing investment tax credit. If the credit equals more than 85% of the gross receipts, compensating and withholding tax liability for the reporting period, the balance of the available credit is carried to the next reporting period.

Interstate Wats Tax Exemption

New Mexico tax law provides for an exemption from interstate telecommunications gross receipts taxes (4.25%) for receipts from the provision of wide-area telephone service (WATS) and private communications services. Therefore, there are no local or state taxes on interstate WATS or private communications services. Wide-area telephone service means a telephone service that entitles a subscriber to either make or receive large volumes of communications to or from persons in specified geographic areas.

Private communications services are dedicated services for a single customer. Furthermore, the service/company entitles the customer to exclusive or priority use of a communication channel or group of channels between a location within New Mexico and one or more specified locations outside New Mexico.

Corporate Income Tax

The Corporate Income Tax is an optional formula for calculating New Mexico corporate income tax liability. The tax is available to corporations primarily engaged in manufacturing. It benefits corporations who have significant investment in plant and payroll in New Mexico, but sell most of their product outside New Mexico. If a company elects to use a double-weighted sales factor, the formula must stay with election minimum of three years.